No. 9270

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

J. H. McCUNE, ALICE W. JACKSON, ALICE P. JACKSON, and FRED D. JACKSON,

Appellants,

vs.

FIRST NATIONAL TRUST AND SAVINGS BANK OF SANTA BARBARA, HORACE P. HOEFER, PETER DAVIDSON, CATHERINE DAVIDSON, and GEORGE GIOVANOLA, Trustee in Bankruptcy, of the Estate of Mortgage Securities, Inc., of Santa Barbara, a Corporation, Bankrupt,

Appellees,

and

J. H. McCUNE, ALICE W. JACKSON, ALICE P. JACKSON, and FRED D. JACKSON,

Appellants,

vs.

THOMAS J. SMITHERAM, E. W. SQUIER, and J. F. GOUX,

Appellees.

APPELLANT'S REPLY BRIEF

Upon Appeals from the District Court of the United States for the Southern District of California, Central Division

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SUBJECT INDEX

TABLE OF CASES AND AUTHORITIES CITED

Pages

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APPELLANT'S REPLY BRIEF

The position and contentions of the Appellants are quite fully set forth in the "Appellants' Opening Brief" which is on file herein. The points and authorities therein set forth will not be here discussed except insofar as necessary to meet any of the arguments and authorities submitted by the Appellees in their brief. A few points

and arguments have been submitted by the Appellees which were not discussed in the "Appellants' Opening Brief," and this reply brief will be devoted principally to a short discussion of such matters.

I.

THE APPELLANTS, AS CREDITORS AND STOCKHOLDERS OF MORTGAGE SECURITIES INC. OF SANTA BARBARA, ARE PROPER PARTIES TO PRESENT THE MOTION TO VACATE THE ADJUDICATION IN BANKRUPTCY.

The Appellees have stated in their Reply Brief that the Appellants, as such stockholders and creditors, have not been prejudiced or damaged by the original adjudication in bankruptcy. Appellees further advance the proposition that the only persons who may move to vacate an adjudication in bankruptcy are persons who have a subsisting interest which may be adversely affected.

It is conceded that J. H. McCune and Alice W. Jackson, Appellants, are creditors of the said Mortgage Securities Inc. of Santa Barbara, and that Fred D. Jackson and Alice P. Jackson, Appellants, are stockholders of Mortgage Securities Inc. of Santa Barbara. The following authorities uphold the right of creditors and stockholders to attack an adjudication in bankruptcy:

AUTHORITIES

In Re: *New York Tunnel Company,* 166 Fed. 284.

Matter of *Free Gold Mining and Milling Company,* 2 Fed. Supp. 118.

Hanna vs. Brictson Mfg. Co., 62 Fed. 2nd 139.

While the Appellants do not concede that it is necessary in order to attack the adjudication in bankruptcy that the Appellants show that they have been, or will be, prejudiced thereby, nevertheless the record shows that the property rights of J. H. McCune, one of the Appellants, have been, or will be, materially affected by the adjudication in bankruptcy. The record shows that J. H. McCune, in two actions pending in the Superior Court of Santa Barbara County, obtained during the period from January 7, to January 12, 1938, attachment liens against real and personal property of Mortgage Securities Inc. of Santa Barbara. (Transcript of Record, pages 7 to 13). As a matter of fact, such attachment liens are made the basis of the original petition in involuntary bankruptcy filed herein, and such petition in involuntary bankruptcy was filed just within four months of the time such liens were obtained, and was obviously filed for the purpose of avoiding such liens.

For the purpose of determining whether or not these attachment liens are avoided by the adjudication in bankruptcy herein, it becomes very material to ascertain the date from which the adjudication in bankruptcy became effective for such purpose. Ordinarily an adjudication

in bankruptcy relates back to the filing of the original petition in bankruptcy, the effect of which is to avoid liens acquired within four months of the date of the filing of such original petition. This rule is predicated, however, upon the premise that the original petition in bankruptcy is sufficient on its face to give jurisdiction. In the event the original petition in bankruptcy is insufficient on its face to give jurisdiction, then the date to which an adjudication in bankruptcy relates for the purpose of avoiding such liens is the date when such original petition in bankruptcy is made sufficient by intervention or otherwise.

The following authorities support this proposition:

AUTHORITIES

Pranta vs. Reich Company, 77 Fed. 2nd 888.
In Re: *Stein,* 130 Fed. 377.
Manning vs. Evans, 156 Fed. 106.
In Re: *Bedingfield,* 96 Fed. 190.
In Re: *Harris,* 299 Fed. 395.
Robinson vs. Hanway, Fed. Case 11953.

It follows, therefore, that the Appellants, especially Appellant J. H. McCune, has a vital interest in the question as to whether or not the original petition in involuntary bankruptcy was sufficient on its face to give jurisdiction, and as to whether or not the original adjudication in bankruptcy should be vacated. If the original petition was insufficient, then the adjudication in bank-

ruptcy should relate only to the time it became sufficient by intervention, if at all, and in such an event the attachment liens of Appellant J. H. McCune are not avoided by the bankruptcy proceedings, as more than four months will have elapsed from the date of such liens to the date the involuntary bankruptcy proceedings became sufficient by proper intervention.

Further too, it is the plain duty of the Court to consider any jurisdictional defects which might make an adjudication void. (In Re: *New York Tunnel Company,* 106 Fed. 284).

II.

THE PURPORTED CREDITOR CLAIMS OF HORACE P. HOEFER AND PETER DAVIDSON AND CATHERINE DAVIDSON DID NOT CONSTITUTE PROVABLE CLAIMS IN BANKRUPTCY, WHICH FACT APPEARED FROM THE FACE OF THE INVOLUNTARY PETITION. THIS IS BY REASON OF THE FACT THAT SUCH CLAIMS ARE SUBROGATION CLAIMS TO ONLY A PORTION OF A LARGER CLAIM, AND BY REASON OF THE FACT THAT SECTION 322a OF THE CIVIL CODE OF THE STATE OF CALIFORNIA, FROM WHICH STATUTORY AUTHORITY SUCH SAID CLAIMS ARISE, IS UNCONSTITUTIONAL AS TO GENERAL CREDITORS OF THE INSOLVENT CORPORATION. THE ORIGINAL

PETITION IN BANKRUPTCY, NOT BEING BASED UPON PROVABLE CLAIMS IN BANKRUPTCY, WAS INSUFFICIENT ON ITS FACE TO GIVE THE DISTRICT COURT ANY JURISDICTION, AND THE ORDER OF ADJUDICATION WAS VOID.

The Court is respectfully referred to pages 17 to 30 of "Appellants' Opening Brief" for the full discussion of these points therein contained.

Appellees make no real attempt in their reply brief to meet the arguments and authorities presented by the Appellants in connection with these points. The Appellees contend, first, that the obligation of the stockholders of Mortgage Securities Inc. of Santa Barbara to pay their proportionate share of the corporate obligations to its creditors was founded on contract. There appears to be no materiality to this point. It is conceded that such liability was founded upon the constitutional and statutory provisions of the laws of the State of California, and that such liability has been defined by the Supreme Court of California as a matter of surety, and therefore of contract. (*Winchester vs. Howard,* 136 Cal. 432). We are not here concerned, however, with the obligation of a stockholder to pay corporate obligations, but with the extent of the right of such stockholder to recover the amount of such payment from an insolvent corporation ahead of or on a par with general creditors.

Appellees then contend, second, that the liability of a stockholder for payment of corporate obligations is direct and primary. Here again, this particular argument, or the cases which purport to support it, appear not to be material. We are not here concerned with the obligation of a stockholder to pay corporate obligations, but only with the extent of the right of such stockholder to recover the amount of such payment from an insolvent corporation ahead of or on a par with general creditors.

Appellees then contend, third, that the right of a stockholder who has paid his proportionate share of his stockholder's liability to be subrogated to the creditor's claim against the corporation is fixed by statute. Here again, there appears to be no question or dispute. It is conceded that prior to the enactment of Section 322a of the Civil Code of the State of California a stockholder who had paid his proportionate share of his stockholder's liability had no cause of action against the corporation for reimbursement. Section 322a of the Civil Code of the State of California purports to give such stockholders a right of subrogation to the portion of the creditor's claim against the corporation which the said stockholders have paid. This right, if constitutional, is undoubtedly fixed by statute. The authorities cited by Appellees in connection with this point are not pertinent in any manner to any of the questions involved in the instant case.

Appellees then contend, fourth, that the subrogation of the stockholder by virtue of Section 322a of the Civil

Code would work no unjust payment out of the assets of the insolvent corporation as between the creditor and the stockholder. The Court is respectfully referred to the "Appellants' Opening Brief" for a full discussion of this matter, and in particular to pages 26 to 29 thereof. Counsel for the Appellees has completely disregarded the fact that, prior to the enactment of Section 322a of the Civil Code of the State of California, a creditor had a vested right to proceed against all of the assets of a corporation for the satisfaction of his claim, as well as directly against the stockholders of the corporation for their proportionate share of the payment of his claim. Obviously, if stockholders who have paid a proportionate share of a creditor's claim are to be subrogated to that creditor's claim against the corporation on an equal basis and footing with the creditor, and if the assets of the corporation are not sufficient for full payment of all claims, then the creditor will have been deprived of a portion of the recourse which he enjoyed prior to the enactment of Section 322a of the Civil Code.

Appellees cite as authority for their contention that Section 322a of the Civil Code of the State of California is constitutional the case of *Patek vs. California Cotton Mills,* 4 Cal. App. 2nd 12. The factual circumstances in the case cited are such, however, as to preclude it from offering any authority in the instant case as to the constitutionality of the Code Section. In the Patek case, as observed by the Court, no one in whose behalf the constitutional questions could be raised was a party, except

the corporation which would not appear to have a right to protect any but its own interest. The complaint in the Patek case alleged that the corporation debtor was solvent, and the Court observed that it must therefore be assumed that it had property sufficient to pay its debts. The holding of the Court in the Patek case is definitely predicated upon the fact that the respondent corporation therein was at all times a solvent going concern. No creditors or creditors' rights were involved in the cited case, and the only point involved was as to whether or not the complaint stated a cause of action as against the corporation. It follows, therefore, that the cited case offers no authority for a determination of the constitutionality of Section 322a of the Civil Code as to a creditor of an insolvent corporation.

III.

THE APPELLANTS WERE NOT GUILTY OF LACHES, AND THE QUESTION OF LACHES IS IMMATERIAL.

In the instant case, the Appellants contend that the question of laches is immaterial, by reason of the fact that the original adjudication in bankruptcy is void, and the original petition for involuntary bankruptcy did not confer jurisdiction upon the Court. As a consequence, the adjudication may be attacked at any time, it being the duty of the Court to inquire into the facts of jurisdiction and act accordingly. It is the duty of the Court, when it believes its jurisdiction may have been imposed

upon, to inquire into the facts and act in accordance therewith. Lack of jurisdiction is a question the Court should consider whenever and wherever raised.

AUTHORITIES

In Re: *Ettinger,* 76 Fed. 2nd 741.

In Re: *Columbia Real Estate Company,* 101 Fed. 965.

The entire question of laches is discussed fully in "Appellants' Opening Brief" at pages 34 to 39 thereof. The Court is respectfully referred thereto for the full discussion of the subject and the authorities cited. The authorities cited by the Appellees may be distinguished in each instance by reason of the factual circumstances involved. In all of the cases cited by the Appellees, the original petition in bankruptcy was sufficient on its face to give the Court jurisdiction. Further too, in all such cases where a petition to vacate an adjudication had been denied for delay, some element of damage, changed condition, acquiesence, acceptance of benefit, etc., existed. In the instant case, the factual circumstances are directly opposite.

CONCLUSION

The "Appellants' Opening Brief" on file herein, together with the within "Appellants' Reply Brief" fully cover all of the points involved, and meet all of the points, arguments, and authorities advanced by the Appellees.

Under the reasoning and authorities presented on behalf of the Appellants, it is again respectfully submitted that the orders of the District Court should be reversed, and that the point raised in the appeal should be definitely determined by this Court.

Respectfully submitted,

T. H. CANFIELD,
Attorney for Appellants.